SUPREME COURT, U.S.
FILED

(1)

No. 98 103

JUL 15 1998
OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

GHAITH R. PHARAON,

Petitioner,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA

PETITION FOR A WRIT OF CERTIORARI

David S. Patterson
Richard F. Lawler
Philip M. Smith
WHITMAN BREED ABBOTT & MORGAN LLP
200 Park Avenue
New York, New York 10166
(212) 351-3000

Kathleen M. Sullivan
Counsel of Record
Crown Quadrangle
Stanford, California 94305-8610
(650) 725-9875

Attorneys for Petitioner Ghaith R. Pharaon

24 PP

QUESTIONS PRESENTED FOR REVIEW

1. Whether a $37 million civil monetary penalty against an individual for omissions under the Bank Holding Company Act is grossly disproportionate in violation of the Excessive Fines Clause.

2. Whether a $37 million civil monetary penalty against an individual under the Bank Holding Company Act that is within the maximum amount permitted by statute but grossly disproportionate to any penalty assessed in a comparable case violates the Due Process Clause.

TABLE OF CONTENTS

		Page
QUESTIONS PRESENTED FOR REVIEW		i
TABLE OF CONTENTS		iii
TABLE OF AUTHORITIES		v
OPINIONS BELOW		1
JURISDICTION		1
CONSTITUTIONAL PROVISIONS INVOLVED . . .		2
STATEMENT OF THE CASE		2
REASONS FOR GRANTING THE WRIT		9
I.	Introduction	9
II.	The Decision Below Violates The Excessive Fines Clause As Interpreted By This Court In *United States v. Bajakajian*	12
III.	The Decision Below Violates The Due Process Clause As Interpreted By This Court In *BMW of North America v. Gore*	16
CONCLUSION		24

TABLE OF AUTHORITIES

Page

CASES

Austin v. United States,
509 U.S. 602 (1993) 13

BMW of North America v. Gore,
517 U.S. 559 (1996) . . . . . *passim*

Hudson v. United States,
118 S. Ct. 488 (1997) 14

Interamericas Investments, Ltd. v. Board of Governors, 111 F.3d 376
(5th Cir. 1997) 19

Long v. Board of Governors,
117 F.3d 1145 (10th Cir. 1997) 9, 19, 20

Pacific Mutual Life Insurance Co. v. Haslip,
499 U.S. 1 (1991) 9

TXO Production Corp. v. Alliance Resources Corp.,
509 U.S. 443 (1993) 17, 18, 20

United States v. Bajakajian, 66 U.S.L.W.
4514 (U.S. June 22, 1998) . . . . . *passim*

In re Vic Sather & Associates, Inc.,
79 Fed. Res. Bull. 160 (1993) 14, 15

Page

STATUTES AND REGULATIONS

12 U.S.C. § 93 14

12 U.S.C. § 1818(h)(2) 6

12 U.S.C. § 1818(i)(2)(G) 4

12 U.S.C. § 1842(a)(1) 3

12 U.S.C. § 1844(c) 3

12 U.S.C. § 1847(b)(1) 4

12 U.S.C. § 1847(b)(5) 3

15 U.S.C. § 2615(a) 11

16 U.S.C. § 5507(a) 11

28 U.S.C. § 1254(1) 2

42 U.S.C. § 9609(b) 11

42 U.S.C. § 11045(b)(2) 11

12 C.F.R. § 225.2(c)(2) 3

12 C.F.R. § 225.5(b) 3

Page

LEGISLATIVE HISTORY

H.R. Rep. No. 95-1383 (1978), *reprinted in* 1978 U.S.C.C.A.N. 9289 14

H.R. Rep. No. 101-54, pt. 1 (1989), *reprinted in* 1989 U.S.C.C.A.N. 90 14

ADMINISTRATIVE POLICY

Interagency Policy Regarding The Assessment Of Civil Money Penalties By The Federal Financial Institutions Regulatory Agencies, 45 Fed. Reg. 59,423 (1980) 5

PETITION FOR WRIT OF CERTIORARI

Petitioner Ghaith R. Pharaon respectfully requests that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the District of Columbia Circuit entered in this case on February 10, 1998, and amended by Order entered April 17, 1998.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the District of Columbia Circuit is reported, as amended, at 135 F.3d 148. The unamended version of that opinion as originally filed on February 10, 1998 is reprinted in the Appendix to this Petition at Pet. App. 1. The April 17, 1998 Order of the Court of Appeals amending its original opinion by deleting several passages is reprinted at Pet. App. 18. The final decision of the Board of Governors of the Federal Reserve System in this case is reprinted at Pet. App. 20. The Recommended Decision of the Administrative Law Judge on which the Board relied is reprinted at Pet. App. 56, and corrections thereto at Pet. App. 193 and 205. The Order of the United States Court of Appeals for the District of Columbia Circuit denying the petition for rehearing is reprinted in the Appendix to this Petition at Pet. App. 209; that court's Order denying the suggestion for rehearing *en banc* is reprinted at Pet. App. 210.

JURISDICTION

The judgment of the United States Court of Appeals for the District of Columbia Circuit in this case was entered on February 10, 1998. A petition for rehearing and suggestion for rehearing *en banc* was timely filed on March 27, 1998, and denied by Order entered April 17, 1998. The opinion filed February 10, 1998 was amended by Order entered April

17, 1998. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISIONS INVOLVED

The United States Constitution, Amendment V, provides, in relevant part, that "No person shall be . . . deprived of life, liberty, or property without due process of law."

The United States Constitution, Amendment VIII, provides that "Excessive bail shall not be required, nor excessive fines imposed, nor cruel and unusual punishments inflicted."

STATEMENT OF THE CASE

This case arises from a decision of the Board of Governors of the Federal Reserve System (the "Board") to impose upon petitioner Ghaith R. Pharaon a civil monetary penalty of $37 million for violations of the Bank Holding Company Act ("BHCA") and associated regulatory reporting requirements -- a sum vastly disproportionate to civil monetary penalties assessed by the Board in comparable cases. While Pharaon does not concede the correctness of the underlying finding of liability, he here seeks this Court's review solely as to the consistency of this penalty with the Eighth Amendment's ban on excessive fines and the Fifth Amendment's guarantee of due process.

In a Notice of Assessment of Civil Money Penalty filed September 13, 1991, the Board charged Pharaon with two kinds of violations of the banking laws. First, it charged that Pharaon, a prominent Saudi Arabian businessman, had participated in the acquisition of a small California bank by the London-based Bank of Credit and Commerce

International ("BCCI") without the prior approval of the Board as required of any company that becomes a bank holding company under Section 3(a) of the BHCA, 12 U.S.C. § 1842(a)(1). Pharaon had acquired the Independence Bank in his own name for $23 million in October 1985. The Board charged that he did so as an undisclosed nominee for BCCI, which had backed the loans with which Pharaon made the purchase, and had entered into an "acquisition agreement" with Pharaon which the Board characterized as giving BCCI a beneficial interest in 85% of Independence shares. The Board charged further that BCCI thereafter effectively controlled Independence through investment of capital and control of the selection of a majority of the bank's directors.

The Board charged, second, that Pharaon had participated in BCCI's failure to disclose its effective control of Independence in annual reports it had filed with the Board as required by the BHCA and the Board's regulation Y. *See* 12 U.S.C. § 1844(c); 12 C.F.R. §§ 225.2(c)(2) & 225.5(b). Even if Pharaon had no actual knowledge of the contents of BCCI's reports, according to the Board, he could be charged with participating in BCCI's reporting omissions under the broad language of 12 U.S.C. § 1847(b)(5), which defines a violation of the BHCA to include "any action (alone or with another or others) for or toward causing, bringing about, participating in, counseling or aiding or abetting a violation."

Without any explanation of how such a figure had been derived, the Board's Notice demanded of Pharaon a civil monetary penalty of $37 million, and sought to prohibit Pharaon from future participation in the banking industry. The Board's enforcement counsel sought to proceed summarily against Pharaon, who had remained outside the United States but denied all charges through his counsel. While the administrative law judge ("ALJ") was prepared to

proceed summarily against Pharaon, Pharaon appealed and the Board, reversing the ALJ, ordered that the matter receive a plenary hearing. After a one-month hearing conducted in 1995, the ALJ issued a recommended decision sustaining all the allegations in the Notice, assessing the $37 million civil monetary penalty that had been requested in the Notice, and issuing an order of prohibition against Pharaon. *See* Pet. App. 56-192.

In arriving at the decision to recommend the $37 million monetary penalty, the ALJ began by calculating the maximum amount that might be assessed under the governing statutes. Prior to the passage of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"), a violation of the BHCA or its implementing regulations was subject to a maximum civil penalty of $1000 for each day the violation continued; after August 10, 1989, the effective date of FIRREA, the maximum daily penalty increased to $25,000 for each day the violation continues. *See* 12 U.S.C. § 1847(b)(1). The ALJ noted that, if each day between Pharaon's acquisition of Independence and issuance of the Notice of Assessment were counted as a separate violation of the Act, and if such liability were cumulative for each separate year that BCCI filed a Y-7 report without reference to Independence, then the statutory maximum liability would total $111.6 million. *See* Pet. App. 161-164.

The ALJ next made reference to the "mitigating factors" required under 12 U.S.C. § 1818(i)(2)(G) to be considered in determining any penalty: "(i) the size of financial resources and good faith of the . . . person charged; (ii) the gravity of the violation; (iii) the history of previous violations; and (iv) such other matters as justice may require." The ALJ asserted that Pharaon must be "an extremely wealthy individual," having declared his net worth

over a decade earlier to be "almost half-a-billion dollars." Pet. App. 168. The ALJ argued further that Pharaon had not shown good faith, had committed grave banking violations, and had made other reporting omissions in connection with the Independence purchase, concluding that no mitigation was in order. Pet. App. 169-176.

Finally, in setting the recommended penalty amount, the ALJ noted, but then expressly declined to rely on, the thirteen mitigating and aggravating factors set forth in the Interagency Policy Regarding the Assessment of Civil Money Penalties by the Federal Financial Institutions Regulatory Agencies, 45 Fed. Reg. 59,423, 59,424-45 (1980) (the so-called "FFIEC" factors). *See* Pet. App. 177-184 (listing the factors as "willfulness," "frequency or recurrence," "continuation of violation," "failure to cooperate," "concealment," "harm to the institution or public confidence," "gain or benefit," "restitution," "prior violations," "previous criticism," "compliance program," "unsafe or unsound practices," and "preventive measures"). The ALJ suggested that he had privately undertaken an application of these factors, "the details of which are not repeated since they resulted in computation of a civil money penalty of slightly over $300 million," Pet. App. 184, an amount he deemed irrelevant since it exceeded the $111 million statutory maximum. In his corrections to the recommended decision filed three days later, the ALJ cut the supposed $300 million in half to $151 million without explanation, as if a change of such magnitude were merely a typographical error, *see* Pet. App. 194, 204.

Summing up his penalty recommendation, the ALJ conceded that, "insofar as the transactions with Independence are concerned, Pharaon did not enjoy any material financial or other benefit." Pet. App. 184. Nonetheless, he concluded, as a matter of what he called "judgmental

rationality," that the penalty against Pharaon should "be limited to less than the maximum of $111 million, but should be not less than one-third thereof, to wit, $37 million, the amount sought in the original Notice." Pet. App. 184. He noted that "collection of this sum is clearly within Pharaon's means" because it was "presumably secured by the predecisional attachment" of Pharaon's assets within the United States. Pet. App. 184; *see id.* at 131 (stating "There has been a predispositional seizure of some $37 million in assets within the United States said to belong to Pharaon").

The Board issued a final decision on January 31, 1997, rejecting all of Pharaon's and the government's exceptions to the ALJ's recommended decision. Concurring in the findings of the ALJ, the Board imposed upon Pharaon both a monetary penalty of $37 million and an order of prohibition. Quoting the ALJ's recommended decision, the Board stated that "'[$37 million] is a very meaningful figure, in line with the gravity of the offenses, the intentional nature of the actions, [and] the attempts to conceal the nature of the transactions that also took into account both Pharaon's financial means and the failure to establish an evidentiary link between Pharaon and the Independence Bank transactions by themselves.'" Pet. App. 34. Like the ALJ, the Board conceded that there had been no showing of the amount of any gains Pharaon had sought or realized from the Independence acquisition, but found it sufficient that there had been some sort of "an overall plan" that had been intended to "yield profits in which Pharaon would share." Pet. App. 35-36.

Pursuant to 12 U.S.C. § 1818(h)(2), Pharaon appealed the Board's decision to the Court of Appeals for the District of Columbia Circuit, which affirmed in all material respects in a decision filed February 10, 1998. With respect to the $37 million monetary penalty, the court of appeals conceded

that "the Board nowhere tells us how its enforcement counsel originally selected thirty-seven million dollars." Pet. App. 14. The court nonetheless rejected Pharaon's argument that the penalty amount was arbitrary or capricious under the Administrative Procedure Act ("APA"), asserting that the "path" of the Board's reasoning could "'reasonably be discerned'" as follows:

> Thirty-seven million dollars reflects the approximate amount the Board found BCCI invested in Independence, as well as approximating the magnitude of the gains sought and the potential harm posed by Pharaon's facilitation of BCCI's secret takeover of a bank worth several hundred million dollars.

Pet. App. 14-15. The court later again referred to "BCCI's unrecoverable investment in the now-defunct Independence" in sustaining the prohibition order against Pharaon. Pet. App. 17. The court asserted this justification for the amount of the penalty despite the fact that the only evidence in the record of the "worth" of Independence was its purchase price of $23 million, not "several hundred million dollars"; despite the fact that there was no evidence in the record of the amount of any "gains" expected by Pharaon from the undisclosed Independence acquisition; and despite the fact that there was no evidence in the record that BCCI had lost money on Independence since there was nothing in the record to suggest that BCCI's loans to Pharaon had not been repaid.

The court of appeals went on to summarily reject Pharaon's arguments that the penalty violated the Excessive Fines Clause of the Eighth Amendment, U.S. Const. Amend. VIII, and the Due Process Clause of the Fifth Amendment, U.S. Const. Amend. V, as interpreted in *BMW of North*

America v. Gore, 517 U.S. 559 (1996). With respect to the excessive fines claim, the court stated that "[a]s we have already indicated in rejecting Pharaon's APA challenge, the penalty is proportional to his violation and well below the statutory maximum." Pet. App. 16. With respect to the due process claim, the court stated simply that "[b]ecause the assessed penalty falls far below the statutory maximum, Pharaon cannot claim that he lacked constitutionally adequate notice." Pet. App. 16.

On March 29, 1998, Pharaon filed a petition for rehearing and suggestion for rehearing *en banc*, arguing, *inter alia*, that the court of appeals' post hoc rationalization for the selection of $37 million as the amount of the penalty lacked any basis in the record. On April 17, 1998, the court of appeals issued orders denying Pharaon's petition for rehearing and suggestion for rehearing *en banc*. *See* Pet. App. 209, 210.

The court of appeals, however, also issued a third order on April 17, 1998, setting forth two remarkable amendments to its original opinion. It ordered the deletion in its entirety of the sentence quoted above, which states "Thirty seven million dollars reflects the approximate amount . . .," and likewise ordered the deletion of the sentence later referring to "BCCI's unrecoverable investment" in Independence. *See* Pet. App. 18-19. In other words, the court of appeals deleted the only sentences in its earlier opinion offering any reasoned basis for the appropriateness of the $37 million penalty amount. Stripped of these sentences, the opinion as amended no longer affords any basis whatever for finding the assessed penalty "proportional to [Pharaon's] violation." Accordingly, the panel's finding that the penalty is constitutional under the Excessive Fines and Due Process Clauses is left to rest solely on the premise that the penalty is below the statutory maximum.

REASONS FOR GRANTING THE WRIT

I. Introduction

The Board's assessment of a $37 million civil monetary penalty against petitioner Pharaon is the paradigm case of an "extreme result that jar[s] one's constitutional sensibilities." *Pacific Mutual Life Insurance Co. v. Haslip*, 499 U.S. 1, 18 (1991). A sum of this order of magnitude is unparalleled in Board enforcement history in comparable cases before or since. As set forth in the record below, the highest civil money penalty assessed by the Board during the period 1990-1994 against any individual for banking violations unconnected to BCCI was $600,000, and the average penalty assessed against any individual during that period was $60,000. *See* Pet. App. 211-215. Thus, the Board singled out Pharaon for a penalty nearly 62 times the next highest amount levied on any like individual and more than 600 times the average individual penalty for that time period.

When the Board's enforcement practice is updated to the present, it is clear that the Pharaon penalty remains an extreme outlier, greater by many orders of magnitude than individual penalties in other similar cases. After 1994, the highest civil money penalty assessed against an individual for banking violations was $717,941, a sum less than one-fiftieth the amount assessed against Pharaon, even in a case involving deliberate and egregious violations of the banking laws. *See* Pet. App. 216; *see also Long v. Board of Governors*, 117 F.3d 1145 (10th Cir. 1997) (affirming the $717,941 penalty). And the average penalty assessed against individuals during this period was just over $44,000, again a trivial fraction of the amount assessed against Pharaon.

To be sure, under an apparent BCCI exception to normal Board practices, three other individuals charged with

BCCI-related banking violations were assessed multimillion-dollar penalties during the 1990-1994 time period. *See* Pet. App. 211 (noting a $35 million penalty assessed in 1993 against Sheikh Khalid bin Mahfouz, a $20 million penalty assessed in 1992 against Kemal Shoaib, and a $10 million penalty assessed in 1992 against Sheikh Kamal Adham). But those penalties are not properly viewed as parallel to the one assessed against Pharaon. In the cases of Sheikh Mahfouz and Sheikh Adham, two other very prominent Saudi Arabian businessmen, these payments were made in connection with the complete settlement of extensive criminal charges filed by the New York District Attorney. And in the case of Shoaib, the assessment was entered on default. Pharaon's assessment, in contrast, is vigorously contested and relates solely to civil banking violations. In any event, even if these cases were viewed as comparable to Pharaon's, they would hardly dispel the issue of whether Pharaon's treatment, as well as theirs, was disproportionate in relation to general Board practice.

Despite the stark and vivid disproportion between the penalty imposed on Pharaon and penalties imposed by the Board in like cases, the decision of the court of appeals as amended treated the Excessive Fines Clause and the Due Process Clause as satisfied virtually *per se* by the fact that $37 million was within the amount authorized by statute -- notwithstanding the absence of any reasonable explanation for how such a figure had been chosen from among all the numbers between zero and $111 million. This decision cannot be squared with this Court's recent holding in *United States v. Bajakajian*, 66 U.S.L.W. 4514 (U.S. June 22, 1998), that grossly disproportionate monetary sanctions violate the Excessive Fines Clause of the Eighth Amendment. Nor can it be squared with this Court's holding in *BMW of North America v. Gore*, 517 U.S. 559 (1996), that the Due Process Clause of the Fifth Amendment invalidates monetary

sanctions whose ratio to actual harm or to sanctions imposed in comparable cases is so "breathtaking" as to suggest the exercise of arbitrariness, caprice, or redistributive opportunism. For either or both of these reasons, this Court should grant the petition and give this case plenary review.

This Court should review the judgment below not only because it subjects Pharaon to grave constitutional error warranting correction in this particular case, *cf. BMW*, 517 U.S. at 586 n.41 (stating that "the fact that this is the first case in decades in which we have found that a punitive damages award exceeds the constitutional limit . . . surely does not justify an abdication of our responsibility to enforce constitutional protections in an extraordinary case such as this one"), but also because it invites recurring constitutional error under the BHCA and numerous similar laws. For the BHCA, like many other federal statutes, permits modest penalties to be multiplied, potentially to the point of abuse, by a factor bearing little relationship to the gravity of the underlying conduct -- here, the number of days a reporting violation continues. *Cf.*, *e.g.*, Toxic Substances Control Act, 15 U.S.C. § 2615(a) (authorizing a penalty of up to $25,000 per day for noncompliance or reporting omissions under environmental laws); High Seas Fishing Compliance Act, 16 U.S.C. § 5507(a) (authorizing a penalty of up to $100,000 per day for noncompliance or reporting omissions under fishing laws); Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. § 9609(b) (authorizing a penalty of up to $25,000 per day for noncompliance or reporting omissions under hazardous waste disposal laws); Emergency Planning and Community Right-To-Know Act, 42 U.S.C. § 11045(b)(2) (authorizing a penalty of up to $25,000 per day, or $75,000 per day in the case of a subsequent offense, for violation of reporting requirements relating to releases of hazardous substances). Under such statutes, the maximum authorized penalty amount

quickly escalates to astronomical sums. A rule that any monetary penalty is *per se* constitutional if below a statutory maximum that may well approach infinity is tantamount to a rule that the Constitution does not apply to such penalties at all.

This Court therefore should grant *certiorari* to clarify the point that monetary penalties that are grossly disproportionate to sanctions in like cases and to any specifically demonstrated harm do not automatically satisfy the Fifth and Eighth Amendments merely because they are within a statutory maximum -- especially where the statutory maximum is elastic and indefinite. Alternatively, this Court at the very minimum should grant the petition and vacate and remand the decision below for reconsideration in light of this Court's intervening decision in *United States v. Bajakajian*.

II. The Decision Below Violates The Excessive Fines Clause As Interpreted By This Court In *United States v. Bajakajian*

The sum total of the court of appeals' response to Pharaon's excessive fine claim in its original opinion was the following: "As we have already indicated in rejecting Pharaon's APA challenge, the penalty is proportional to his violation and well below the statutory maximum." Pet. App. 16. After the court's order of April 17, 1998 deleted the sole sentence in its original opinion stating how Pharaon's penalty might be sufficiently "proportional" to defeat his APA challenge, *see* p. 8 *supra*, the court's only remaining rationale for the constitutionality of the penalty under the Excessive Fines Clause was that $37 million was below the statutory maximum. But such a premise of *per se* constitutionality plainly conflicts with this Court's intervening decision in *United States v. Bajakajian*, 66 U.S.L.W. 4514 (U.S. June 22, 1998).

In *Bajakajian*, this Court for the first time held a monetary sanction unconstitutional under the Excessive Fines Clause. The Court had long noted that "[t]he Excessive Fines Clause limits the government's power to extract payments . . . 'as punishment for some offense.'" *Austin v. United States*, 509 U.S. 602, 609-10 (1993) (quoting *Browning-Ferris Industries v. Kelco Disposal, Inc.*, 492 U.S. 257, 265 (1989)). But *Bajakajian* clarified for the first time that the test for determining if a punitive civil sanction violates the Excessive Fines Clause is whether "it is grossly disproportional to the gravity of a defendant's offense." 66 U.S.L.W. at 4518.

Applying this test, *Bajakajian* held that a defendant could not constitutionally be forced to forfeit the entire sum of $357,144 in currency that he was trying to take out of the country without complying with currency reporting laws. Writing for the Court, Justice Thomas held that this forfeiture was punitive for purposes of the Excessive Fines Clause, *see id.* at 4516, and that a penalty in such an amount was grossly disproportional to the offense of "a willful failure to report the removal of currency from the United States". *Id.* at 4519. As Justice Thomas wrote, the forfeiture was larger "by many orders of magnitude" than the $5000 maximum fine authorized in the defendant's circumstances by the United States Sentencing Guidelines, and bore "no articulable correlation to any injury suffered by the Government." *Id.* Justice Thomas deemed it irrelevant that Congress and the Sentencing Commission had expressly authorized the forfeiture in addition to the fine, reasoning that a sentencing guideline permitting a forfeiture mandated by statute "cannot override the constitutional requirement of proportionality review." *Id.*

The Excessive Fines Clause plainly applies to civil monetary penalties under the BHCA just as it did to the *in*

personam forfeiture in *Bajakajian*. Just last Term, this Court specifically suggested that, even if civil money penalties assessed under the National Bank Act, 12 U.S.C. § 93, did not constitute an "offence" for purposes of the Double Jeopardy Clause, they were nonetheless subject to "[t]he Eighth Amendment['s] protect[ion] against excessive civil fines." *Hudson v. United States*, 118 S. Ct. 488, 495 (1997).

Moreover, even if civil monetary penalties must be specifically shown to be "punitive" in order to trigger the ban on excessive fines, there can be no doubt that penalties under the BHCA meet that standard. Like the *in personam* forfeiture in *Bajakajian*, BHCA penalties are imposed as punishment designed to deter and to achieve retribution, not as remedies to compensate the government for loss. When first enacted in 1978, civil monetary penalties under the banking statutes were intended to "serve as deterrents to violations of laws, rules, regulations, and orders of the [banking] agencies." H.R. Rep. No. 95-1383, at 17 (1978), *reprinted in* 1978 U.S.C.C.A.N. 9289. When those penalties were increased by FIRREA in 1989, they were intended to strengthen federal enforcement power against banking "fraud or insider abuse," H.R. Rep. No. 101-54, pt. 1, at 294, 300 (1989), *reprinted in* 1989 U.S.C.C.A.N. 90, 96, and, in light of crippling backlogs in bank fraud investigations in the federal criminal justice system, *see id.* at 464-65, *reprinted in* 1989 U.S.C.C.A.N. 260-61, to "give[] the regulators . . . the tools which they need . . . to punish culpable individuals," *id.* at 466, *reprinted in* 1989 U.S.C.C.A.N. 262. The Board's own statements likewise routinely confirm that it understands civil monetary penalties as serving punitive rather than remedial functions. *See, e.g., In re Vic Sather & Associates, Inc.*, 79 Fed. Res. Bull. 160, 164 (1993) (noting that "an assessment of a penalty under the BHC Act serves the purposes of deterring repeat violations

by the Respondents (specific deterrence) and acting as a warning to other similar bank holding companies and individuals (general deterrence)").

Under the Excessive Fines Clause as interpreted in *Bajakajian*, the decision below cannot stand. Here, as in *Bajakajian*, the overwhelming bulk of the basis for the penalty amount -- the cumulative daily penalties from the omission of mention of Independence in BCCI's Y-7 reports -- stems from what was "solely a reporting offense." 66 U.S.L.W. at 4519. Here, as in *Bajakajian*, the government was deprived "only of the information" about the ownership of Independence, not of any demonstrated "loss to the public fisc." *Id.* Here, as in *Bajakajian*, the penalty amount was wildly disproportional to the culpability level the government had otherwise given notice it attached to the misconduct -- there, through the $5000 fine provided for in the Sentencing Guidelines, *id.*, and here, through the settled practice of assessing penalty amounts no greater than $600,000 to $700,000 in comparable cases. And here, as in *Bajakajian*, it is no defense that Congress has expressly authorized the penalty, for here, as in *Bajakajian*, such statutory authorization "cannot override the constitutional requirement of proportionality review." *Id.* n.14.

The proportionality review that is constitutionally required under *Bajakajian* remains to be undertaken in this case. The Board expressly declined to rely on "proportionality tests that . . . compare the size of the penalty with the size of any actual damages or government loss," choosing instead to examine merely the "'nature of the conduct.'" Pet. App. 43. Upon reaching the conclusory judgment that Pharaon's conduct was "fully intentional, continuing and extremely serious," the Board made no further inquiry into whether the unprecedented $37 million penalty against him might constitute an excessive fine. The

test applied by the Board is obviously incorrect as a matter of law after *Bajakajian*. And whatever proportionality review the court of appeals undertook in its original opinion was utterly wiped out by its order amending its decision. The court's apparent residual conclusion that a fine is *per se* constitutional if authorized by Congress is plainly contradicted by *Bajakajian*. *Bajakajian* held that statutory authorization does not automatically defeat an excessive fines claim and required appellate courts to review excessive fines claims *de novo* for proportionality based on all relevant facts. 66 U.S.L.W. at 4519 n.10. As amended, the court of appeals' opinion entirely abdicated this constitutional duty.

For these reasons, this Court should grant the petition and apply the appropriate proportionality review to the extraordinary penalty levied against Pharaon in this case. Alternatively, this Court at least should grant, vacate and remand the decision to the court of appeals for reconsideration in light of *Bajakajian*.

III. The Decision Below Violates The Due Process Clause As Interpreted By This Court In *BMW of North America v. Gore*

The court of appeals summarily rejected Pharaon's due process objections to the $37 million penalty with the simple pronouncement that "[b]ecause the assessed penalty falls far below the statutory maximum, Pharaon cannot claim that he lacked constitutionally adequate notice." Pet. App. 16. With all respect, such a mechanical approach to due process is inconsistent with this Court's precedents and accordingly merits this Court's review.

In *BMW of North America v. Gore*, 517 U.S. 559 (1996), this Court invalidated as grossly excessive a jury award of punitive damages against a tortfeasor, holding that

the guarantee of due process imposes outer limits on disproportionate or arbitrary monetary penalties. As Justice Stevens wrote for the majority: "Elementary notions of fairness enshrined in our constitutional jurisprudence dictate that a person receive fair notice not only of the conduct that will subject him to punishment, but also of the severity of the penalty that [government] may impose." *Id.* at 574. As the Court made clear in *BMW*, a punitive damages award of $2 million for a $4000 concealed paint job -- involving as it did a "breathtaking 500 to 1" ratio between penalty and actual harm, *id.* at 583 -- did not afford such fair notice and thus was unconstitutional.

The Court in *BMW* expressed two related but distinct concerns about such excessive punitive damage awards. First, the Court noted that such awards offend notions of proportionality with deep roots in the common law. *See id.* at 580 ("The principle that exemplary damages must bear a 'reasonable relationship' to compensatory damages has a long pedigree."); *see also TXO Production Corp. v. Alliance Resources Corp.*, 509 U.S. 443, 476-79 & nn.1-3 (1993) (O'Connor, J., dissenting). This concern is a substantive one that looks to whether the amount of the penalty is excessive in relation to the harm caused -- a consideration similar to the one the Court expressed in interpreting the Excessive Fines Clause of the Eighth Amendment in *Bajakajian*.

Second, quite apart from any substantive concern with proportionality, the Court in *BMW* viewed excessive punitive damages awards as likely to reflect procedures that are inconsistent with the rule of law. As Justice Stevens emphasized in the majority opinion, due process requires that a penalty be foreseeable in amount. A punitive damages award that departs sharply from settled practice in comparable cases cannot afford such predictability. Moreover, an unforeseeable penalty raises the dangers of

arbitrary and selective treatment. As Justice Breyer, joined by Justices O'Connor and Souter, wrote in concurrence in *BMW*: "Requiring the application of law, rather than a decisionmaker's caprice, does more than simply provide citizens notice of what actions may subject them to punishment; it also helps to assure the uniform general treatment of similarly situated persons that is the essence of law itself." 517 U.S. at 587 (Breyer, J., concurring). *See also TXO*, 509 U.S. at 466-67 (Kennedy, J., concurring in part and concurring in the judgment); *id.* at 472-73 (O'Connor, J., dissenting) (noting that the Due Process Clause requires limits on the role of arbitrary or irrelevant factors in jury discretion).

For either or both of these reasons, the $37 million penalty that the Board assessed against Pharaon, like the punitive damages award invalidated in *BMW*, is excessive, in violation of due process. Whether measured by "the disparity between the harm or potential harm" demonstrated and the amount of the penalty, *see BMW*, 517 U.S. at 575, or by "the difference between this remedy and the civil penalties . . . imposed in comparable cases", *see id.*, a $37 million penalty for BHCA omissions is wildly disproportionate. And neither the Board nor the court below has offered any articulable basis for the disparity.

To begin with, the staggering difference between the Board's treatment of Pharaon and its treatment of his counterparts in non-BCCI cases cannot be explained by different degrees of reprehensibility in their underlying conduct. *See id.* (listing "reprehensibility" as a relevant guidepost). For the BHCA penalty provisions contain no requirement of scienter, and, while the ALJ and the Board made conclusory findings that Pharaon had been conscious of wrongdoing, other individuals found by the Board to have

engaged in intentional and even flagrant misconduct have received penalties a fraction as large.

For example, in *Interamericas Investments, Ltd. v. Board of Governors*, 111 F.3d 376 (5th Cir. 1997), a case involving deliberate and egregious reporting omissions by a foreign bank holding company, the Board assessed penalties of only $1 million against the company and $10,000 against the individual. The Board has never explained why Pharaon's reporting omissions should be penalized in an amount 370 times as high. Nor can any difference in "reprehensibility" explain why Pharaon was penalized 52 times as heavily as the individual in *Long v. Board of Governors*, 117 F.3d 1145, 1156 (10th Cir. 1997) (affirming a $717,941 BHCA penalty for engaging deliberately in an unapproved bank merger and refusing to reverse the transaction despite repeated warnings from banking officials, finding "$567,941 [to be] necessary to deprive [the defendant] of the fruits of his unlawful conduct," and "a $150,000 penalty [to be] essential to deter future misconduct").

Nor can the explanation be found in any greater degree of harm caused by Pharaon's actions. For as the court of appeals' telling amendment of its opinion confirms, there is not, and has never been in this case, any demonstration of any dollar figure for any harm supposedly caused by the omissions charged against Pharaon, whether $37 million or any other amount. Nor did the government demonstrate any amount of unjust enrichment to Pharaon that might have justified disgorgement or restitution, a fact that both the ALJ and the Board expressly noted.

Nor can Pharaon's personal wealth, which the Board presumed to be considerable based on a then decade-old admission, supply the reason for the vastly different penalty

imposed upon him. As this Court noted in *BMW*, the fact that one is wealthy rather than "impecunious" does not diminish one's "entitlement to fair notice." 517 U.S. at 585. And as Justice Breyer cautioned in his concurrence, wealth ought not be used as "an open-ended basis for inflating awards." *Id.* at 591 (Breyer, J., concurring). *See also TXO*, 509 U.S. at 487-95 (O'Connor, J., dissenting) (noting the danger that an emphasis on a defendant's financial resources may tempt juries to engage improperly in the arbitrary redistribution of wealth). In any event, the governing statute permits "the size of financial resources" to be used only as a mitigating factor, not as a starting point for setting a penalty grossly disproportionate to any assessed in a comparable case.

Surely the fortuity that the government had attached $37 million of Pharaon's assets prior to this proceeding, *see* Pet. App. 131, 184, cannot suffice to justify a penalty in precisely that amount. Due process requires far more than a rule of finders-keepers. *Cf. Bajakajian*, 66 U.S.L.W. at 4519 (finding "no inherent proportionality" in the government's keeping precisely the amount of the defendant's currency it had in hand).

Concerns to effect deterrence likewise cannot explain the disproportionate penalty imposed upon Pharaon. Specific deterrence of future misconduct by Pharaon himself is hardly a relevant consideration in an action prohibiting him from future participation in the United States banking industry. And there is no reason why general deterrence of reporting violations under the banking law could not be achieved by setting the penalty at an amount sufficient to discourage the person of less than extraordinary wealth. *Cf. Long*, 117 F.3d at 1156 (finding a mere $150,000 penalty component sufficient "to deter future misconduct"). As Justice Stevens noted in *BMW*, "[t]he sanction imposed in this case cannot be

justified on the ground that it was necessary to deter future misconduct without considering whether less drastic remedies could be expected to achieve that goal." 517 U.S. at 584.

Thus the one and only source of supposed constraint on the unfettered and unguided exercise of Board discretion in this case is the fact that $37 million was within the maximum authorized by the governing statute, read to permit successive and cumulative daily penalties for the same misconduct over a period of years. As amended, the court of appeals' decision below must be read to set forth a *per se* rule that any penalty under the BHCA is consistent with due process if below the statutory maximum, no matter how dramatically that penalty departs from amounts assessed in parallel matters under settled administrative practice. But such a *per se* rule cannot be reconciled with due process as interpreted in *BMW*.

To be sure, the Court in *BMW* acknowledged the relevance of legislative judgments of the appropriate level of civil sanctions, finding that the punitive damage award at issue there was lawless in part because it exceeded the maximum civil penalties authorized by the state legislature for comparable conduct. And to be sure, the $25,000 per day penalties authorized under the BHCA as amended by FIRREA reflect Congress's judgment that maintaining the integrity of the banking system is extraordinarily important.

But the statute at issue here is a far cry from the sort of statute referred to as a source of due process guidance in *BMW*. Unlike a statute setting forth a fixed ceiling for a penalty amount, such as a maximum dollar figure or a maximum percentage of net worth, the BHCA sets forth only a daily maximum that may be cumulated indefinitely. Such a sanction, when applied to reporting violations that endure over several years, rapidly escalates to astronomical sums far

beyond any specific contemplation attributable to Congress. If Congress had authorized civil sanctions without limit, it would hardly be consistent with due process for an agency to assess penalties in the amount of infinity. A statute allowing the indefinite cumulation of penalties likewise cannot foreclose inquiry into whether any given penalty falling within its wide range is consistent with due process.

Put another way, a statutory penalty scheme allowing penalties that rapidly cumulate to astronomical sums should be understood as delegating to the implementing agency the constitutional responsibility of articulating standards that will allow consistent and non-arbitrary treatment of offenders within the monetary ranges that are practically realistic. On this score, the Board's performance in this case was severely wanting. While the Board is bound to consider the thirteen FFIEC factors in penalty determinations, as the court of appeals held, *see* Pet. App. 14, the ALJ's private "computation" of the appropriate penalty amount under those factors was so unsystematic that it apparently yielded a sum of $300 million one day and $151 million the next. "Factors" that do so little to constrain open-ended discretion are not enough to satisfy due process. *Cf. BMW,* 517 U.S. at 589-92 (Breyer, J., concurring) (finding a seven-factor test set forth by the Alabama Supreme Court too vague and open-ended to cabin the jury's discretion as required by due process).

In short, the Board in this case chose the penalty amount with free-floating discretion, and not subject to any genuinely constraining rule of law. Without some articulable connection to a theory of retribution, deterrence, or restitution, the Board's sharp deviation from historical practice in singling out Pharaon for an astronomical sanction amounts to the very sort of arbitrary behavior condemned in *BMW* -- not the exercise of law, but of "a decisionmaker's

caprice". *Id.* at 587. Without any reasoned theory of how $37 million is proportional to some harm done to Independence, BCCI or the United States banking system, that sum is for all intents and purposes chosen at random.

The application of due process to civil monetary penalties is an important issue not only for those subject to the multiple daily penalties of the BHCA as amended by FIRREA, but for all those subject to any similar multiple or cumulative penalty scheme authorized by federal statute. *See* pp. 11-12 *supra*. The court of appeals' *per se* rule immunizing from due process review any penalty amount below the statutory maximum in such a scheme cannot be reconciled with due process or the rule of law. Because of the grave constitutional injustice to Pharaon in this case, the stark conflict between the decision below and this Court's decision in *BMW*, and the potential importance of the erroneous ruling below across a wide range of statutes involving highly elastic penalty structures, this Court should grant review in this case.

CONCLUSION

For these reasons, Petitioner respectfully requests that this Court grant the petition and give plenary review to the decision below. In the alternative, Petitioner respectfully requests that this Court grant the petition, vacate the decision below, and remand to the court of appeals for reconsideration in light of this Court's intervening decision in *United States v. Bajakajian*.

Dated: Stanford, California
July 14, 1998

Respectfully submitted,

Kathleen M. Sullivan
Counsel of Record
Crown Quadrangle
Stanford, CA 94305-8610
(650) 725-9875

David S. Patterson
Richard F. Lawler
Philip M. Smith
WHITMAN BREED ABBOTT & MORGAN LLP
200 Park Avenue
New York, New York 10166
(212) 351-3000

Attorneys for Petitioner
Ghaith R. Pharaon